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STATE FOR EAP/CM AND EEB/OMA, TREASURY FOR OASIA

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TAGS: ECON EFIN EINV ETRD HK CH
SUBJECT: Tsang Policy Address Warns of Tough Times Ahead, Hang Seng
Falls 5 percent

REFS: A) HONG KONG 1886, B) HONG KONG 1875

¶1. Summary: After a strong rebound on Monday and Tuesday, the Hang Seng Index slipped on Wednesday to close at 15988.30, down 834 points or 4.96 percent on the day. HIBOR fell slightly, but remained high. The British government's announcement that it would inject capital into the banking sector appeared to improve market sentiment earlier in the week, but a similar announcement by the U.S. does not appear to have been enough to sustain the gains of recent days. In his annual Policy Address to the Legislative Council (LegCo) today, Hong Kong Chief Executive Donald Tsang warned of tough times ahead, but promised increased fiscal measures to help Hong Kong see its way through the financial turbulence. Financial Secretary John Tsang continued to warn of impending economic turmoil and an economic recession in 2009. Financial Secretary Tsang and HKMA Chief Executive Joseph Yam jointly announced late Tuesday that the Hong Kong government would immediately guarantee all bank deposits and provide supplementary capital to banks as necessary. These two new measures would be effective until the end of 2010. End Summary.

CE Tsang's Policy Address Promises New Task Forces

¶2. Hong Kong Chief Executive Donald Tsang's annual Policy Address to the Legislative Council focused on steps the government would take to protect the economy from the worst effects of the global financial crisis. Tsang said he would chair a new task force to monitor and assess the impacts of the financial "tsunami" on local and global markets. Members will include top government officials, financial experts, economists and representatives of major industries in Hong Kong. Tsang told the LegCo that the destructive force of the current financial crisis is greater than the 1997 Asian Financial Crisis. In the wake of fears that AIG subsidiary AIA might come under pressure, Tsang also proposed the establishment an independent Insurance Authority to improve supervision of the insurance industry. Hong Kong is one of the only economies in the region that does not currently have an independent insurance regulator.

¶3. Tsang also promised government action on the Competition Bill and Minimum Wage proposals during the coming legislative session. He announced that his Labor and Welfare Bureau will establish a minimum wage commission to study the appropriate minimum wage level that could apply across all industries. Tsang called on the Hong Kong people to stay calm in spite of global financial volatility. He promised that the government would intervene if the market fails, taking remedial measures when the market is unable to resolve disputes between "big business and ordinary citizens." Observers took his remarks to mean the government would continue to pressure banks to resolve claims surrounding Lehman minibonds.

Hang Seng Not Impressed

¶4. Investors were not encouraged by Tsang's address. The Hang Seng Index lost 4.96 percent or 834.58 points on Wednesday, closing at 15998.30 with a daily trade of HKD 49 billion. The market had rebounded strongly on Monday and Tuesday after British Prime Minister Gordon Brown announced plans for the UK government to purchase stakes in British banks. The Hang Seng gained 10 percent on Monday and 3 percent on Tuesday, when markets heard that the U.S. would unveil a similar plan to recapitalize banks. HIBOR quoted by Hang Seng Bank at 5:13 pm was 2 percent for overnight, 3.0 percent for 1W, 3.5 percent for 2W, 4.5 percent for 1M, 4.35 percent for 3M and 4.05 percent for 6M.

Hong Kong Follows UK Lead, Guarantees Deposits
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¶5. Late on Tuesday, HKMA Chief Executive Joseph Yam and Financial Secretary John Tsang announced that the Hong Kong Government would use the HKMA Exchange Fund to immediately guarantee all deposits in the banking system and would provide capital to banks as needed, through 2010. Hong Kong previously had a deposit insurance scheme capped at HKD 100,000 (apx. US$12,800); LegCo members have recently called for that limit to be increased. Hong Kong banks hold HKD 6 trillion (US$ 770 billion) in deposits, well over the Exchange Fund assets of HKD 1.6 trillion (US$ 200 billion). HKMA's Yam told the press that the HKMA was following the lead of other governments not because of concerns about banking system health, but to avoid putting Hong Kong at a competitive disadvantage vis-`-vis other economies that have provided similar guarantees. Yam reaffirmed that Hong Kong banks are healthy and well capitalized and predicted that the Exchange Fund resources would not be tapped.
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